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RUEHBJ/AMEMBASSY BEIJING 2176
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RUEHBUL/AMEMBASSY KABUL 0576
RUEHKT/AMEMBASSY KATHMANDU 0269
RUEHNE/AMEMBASSY NEW DELHI 0437
RHEFDIA/DIA WASHDC
RUEAIIA/CIA WASHDC
RUEKJCS/OSD WASHDC
RHEHNSC/NSC WASHDC
RUCPDO/USDOC WASHDC 0593
RUEKJCS/SECDEF WASHDC
RUEKJCS/JOINT STAFF WASHDC
RUEHGV/USMISSION GENEVA 0621
RUEHVEN/USMISSION USOSCE 2583
RUCNDT/USMISSION USUN NEW YORK 1962
RUEHNO/USMISSION USNATO BRUSSELS BE
RUEHBS/USEU BRUSSELS
RUEHLMC/MILLENNIUM CHALLENGE CORP
RUMICEA/USCENTCOM INTEL CEN MACDILL AFB FL

C O N F I D E N T I A L SECTION 01 OF 02 BISHKEK 000631

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DEPT FOR SCA/CEN (GEHRENBECK)

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TAGS: [ECON](#) [EFIN](#) [KG](#)

SUBJECT: KYRGYZSTAN PASSES 2007 BUDGET

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Classified By: Ambassador Marie Yovanovitch for Reasons 1.4 (b) and (d)

11. (U) Summary: On May 2, President Bakiyev signed Kyrgyzstan's 2007 budget. The 2007 budget projects a 12% increase in expenditures over the 2006 budget, with expenditures reaching \$842 million. The government plans to cover the projected \$105 million deficit by issuing treasury bills and selling state property among other measures. The 2007 budget introduces a "two-tier" system, with direct transfers from the national budget to local administrations. This system, which bypasses oblast and district level administrations, represents a significant step forward in administrative decentralization. A provision included in the 2007 budget requires any cabinet minister who fails to implement his ministry's budget to resign. The budget also stipulates that the government must obtain parliament's approval before making any changes. End summary.

General Budget Overview

12. (U) The Kyrgyz Parliament adopted the 2007 state budget on April 5, and President Bakiyev signed the budget bill into law on May 2. Estimated budget expenditures will increase by 12% over 2006 figures, reaching \$842 million, or 21.4% of projected gross domestic product. The main budget expenditures are: general state services) 34.6%; economic programs) 16.3% social protection - 12.8%; health) 9.6%; public order and security) 8.9%; education) 8.1%; public utilities) 3.8%; defense) 3.5%; recreation, culture and religion) 1.7%; and environmental protection) 0.7%.

13. (U) Budget revenues are projected at approximately \$737

million, with \$618 million in tax revenues and \$119 million in non-tax income. Government measures aimed at legalizing the substantial shadow economy, such as reducing profit tax from 20% to 10% and canceling the 20% VAT on equipment imports, while eliminating several minor taxes and fees, yielded a projected increase over 2006's budget revenues of \$658 million.

¶4. (U) The government plans to cover the projected \$105 million deficit by issuing state treasury bills, privatizing some state property, collecting additional taxes and customs fees and attracting foreign grants and loans. The Kyrgyz government may pursue the privatization of Ayil Bank, which specializes in issuing small loans to rural residents, and Kyrgyz Telecom.

Two Tier Budget

¶5. (U) The 2007 budget was designed on a "two-tier" basis, with direct payments from the national budget to local administrations. This step empowers local self-governance, but requires redirection of some revenues. For example, profit, non-resident, VAT, emergency situations and excise taxes that were previously shared between the local and national budgets, are now completely transferred to the national budget. But income, patent and small entrepreneurship taxes will now be directed only to local budgets. Local officials may have serious difficulties with the new budget system due to the lack of budgeting expertise among their employees. The World Bank, the European Union and USAID have established training programs for issues related to decentralization.

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Other Innovations

¶6. (U) According to provisions included in the 2007 budget, ministers are required to resign if they fail to implement their ministry's budget. In another significant development, the Kyrgyz government must obtain parliamentary approval before making any budgetary changes.

Comment

¶7. (C) It is clear that one way the Kyrgyz are thinking of making up the budget deficit is additional compensation for use of Manas Airbase, as well as greater direct budget subsidies from donors in general, in addition to the United States. We believe that the May 31 Development Forum will be one venue where the Kyrgyz will request more assistance from the donors, including debt relief.
YOVANOVITCH